In the

Supreme Court of the United States

October Term, 1958

No. 38

RAILWAY EXPRESS AGENCY,
INCORPORATED,

Appellant,

v.

COMMONWEALTH OF VIRGINIA,

Appellee.

Appeal from the Supreme Court of Appeals of Virginia

REPLY BRIEF OF APPELLANT IN OPPOSITION TO APPELLEE'S MOTION TO DISMISS AND TO ITS BRIEF IN SUPPORT OF THE MOTION TO DISMISS

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MOTION TO DISMISS

Appellant submits for reasons discussed in its "Statement as to Jurisdiction" and for those assigned in the following reply brief that both questions involved in this appeal are

substantial Federal questions and that the second question so presented rests on no adequate non-Federal basis.

Appellee's Motion to Dismiss should therefore be denied.

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March 31, 1958

REPLY BRIEF OF APPELLANT

Appellant, in replying to the arguments advanced in the brief filed on behalf of Appellee, will discuss such of them as seem material under the same headings and, as far as practical, in the same order in which they are dealt with by counsel for Appellee. Unless otherwise stated all italics are supplied.

Statement of the Case

Appellee contends that the statement of the case included in Appellant's statement as to jurisdiction "requires amplification" and "is in error" in several respects.

1.

Appellant Should Not Be Taxed "as Though" It Were Doing an Intrastate Business

Appellee contends by way of "amplification" that the facts recited on page 5 of its brief raise the question whether, notwithstanding its stipulation that Appellant "conducts only an interstate business in Virginia", it should be taxed as though doing an intrastate business in this State.

The stipulation referred to was entered into by counsel for Appellant, for the Commonwealth and for the State Corporation Commission, prior to the hearing before the Commission and was introduced and considered by it as a part of the evidence in the case. All the facts now referred to by Appellee were, therefore, before the Commission which considered them in the light of the stipulation.

In the light of them the Commission unanimously decided that:

"The peculiar feature of this case is that the Railway

Express Agency *does no intrastate business in Virginia*". (Italics by the Commission)

Moreover, the Commission, in its opinion from which the former appeal was perfected, heard and decided by the Virginia Court in 1953, [194 Va. 757], reached the same conclusion. It said:

> *"The Delaware corporation created and uses the Virginia corporation not for the purpose of getting around the law but for the purpose of obeying the law.* We therefore hold that the corporate entity cannot properly be ignored and that the Delaware corporation is *engaged only in interstate business in the State of Virginia* . . ." (SCC Reports, 1952, p. 34)

In view of the foregoing holding, counsel for Appellant, an Assistant Attorney General for the Commonwealth and counsel for the Commission made a part of the records (Nos. 436 and 437) before the Virginia Court on *that* appeal a stipulation reading as follows:

> *"4. Since the Commonwealth admits and the Commission has found that the taxpayer does no intrastate business in Virginia, the testimony and exhibits relating to that issue are not material on this appeal".*

The "testimony and exhibits" relating to the manner in which both Appellant and the Virginia Company did business in Virginia had been fully developed in the hearings before the Commission *in that proceeding* and embraced all of the facts, among many others, presently referred to by Appellee on this appeal.

In the light of the record *then* before it and the stipulation above referred to, the Virginia Court had this to say on the prior appeal as to the nature of Appellant's business:

"Railway Express Agency, Incorporated, a Delaware corporation, is engaged in the handling and transportation of goods, wares and merchandise in express service in both interstate and intrastate commerce in the District of Columbia and in all the States of the Union except Virginia, *where it does solely an interstate business. Its intrastate express business in this State is carried on by a wholly-owned subsidiary, Railway Express Agency, Incorporated, of Virginia, a Virginia corporation, organized on October 20, 1931,* following the affirmance by this Court of an order of the State Corporation Commission which *denied the appellant the authority to do an intrastate express business in this State*". (194 Va. 757, 759)

When the case was before this Honorable Court on the prior appeal (October term, 1953), (record No. 163), the last mentioned stipulation again appeared in the record (page 20).

While it is true, therefore, that the facts referred to on page 5 of Appellee's brief "were not considered by this Court in the prior case" (Br. p. 13), they were not brought before it because Appellee admitted both before the Commission and the Virginia Court that *notwithstanding them* Appellant "does no intrastate business in Virginia".

The nature of Appellant's business has heretofore been before the Commission and the Virginia Court since 1929 (153 Va. 498), and it has never heretofore been contended that while engaged solely in interstate commerce, Appellant should be taxed "as though" it was engaged in intrastate commerce in Virginia. Such a suggestion implies that Appellant is doing indirectly what Section 163 of the Constitution says and what the Virginia Court held in *Railway Express Agency, Incorporated* v. *Commonwealth* (1929), 153 Va. 498 [a holding which was affirmed by this Court in

1931 (282 U. S. 440)], it may not do directly, namely, conducting the business of a public service corporation in intrastate commerce in this State. The Commission's opinion in the former case (SCC Reports 1952, p. 34) heretofore quoted from in this discussion *expressly decided* that the Virginia Company was organized by Appellant for the purpose of obeying, not violating the law. The Virginia Court affirmed that decision (194 Va. 759).

The *method* of operation employed by the Delaware and Virginia Companies has no bearing on the *nature* of the business transacted by either company. The Delaware Company uses the joint facilities for the transaction of its interstate business and the Virginia Company uses such facilities for the transaction of its intrastate business. *The nature of the business conducted by each is in no way affected by the facilities or personnel employed for that purpose.*

It is therefore respectfully submitted: (a) that Appellee, having "admitted" in the *former* proceeding and having "stipulated" in the *present* proceeding that Appellant does "only an interstate business" in Virginia; (b) that the Commission having *twice* found, *without objection from the Commonwealth,* that Appellant does "only an interstate business" in Virginia, the first of which findings were affirmed by the Virginia Court on the former appeal; and (c) that, *since no cross-error was assigned to the Commission's failure to decide otherwise in the instant case,* Appellee should not now be heard to contend that, notwithstanding the interstate nature of its business, Appellant should, because of its ownership and control of the Virginia Company and their joint use of property and personnel, be taxed "as though" it did an intrastate business in Virginia.

2.

The Incidence of the Tax Is the Same

Appellee takes exception to Appellant's statement that the effect of the 1956 amendment "was to change the nature but not the incidence of the tax" (Brief p. 6). Prior and subsequent to the amendment in question the incidence of the tax was and is *the gross receipts which the Commission found Appellant had derived from its interstate commerce.* Prior and subsequent to such amendment the tax was and is levied *in direct proportion to the extent to which the Commission has found that the privilege of carrying on Appellant's interstate business is exercised in Virginia.* Since the tax must be paid regardless of whether the company owns property in Virginia or not, or whether its operations are conducted at a profit or a loss, the tax is necessarily on the privilege of doing an interstate express business and nothing else. In its practical operation, the tax, therefore, is as the Commission, in its assessment stated it to be, upon "Gross Receipts to be taxed" in the amount of $6,499,515.00.

3.

Appellant's Gross Receipts No Proper Measure of the Value of Its Operating Contracts or Ownership of the Virginia Company.

Appellee also asserts that Appellant's contention that the tax constitutes a taking of its property without due process of law fails to recognize that (a) its existing contracts with railroads granting exclusive privileges to transport express matter over their lines and (b) its ownership of the entire capital stock of the Virginia company, are elements of property which Appellant has not considered in stating the value of its intangible property subject to State taxation.

If either or both of these elements of intangible property have value, there is nothing in the record to show *what* the Commission determined that value to be. Presumably, the Commission meant to decide, at least as to the value of Appellants contracts with the railroads, that they represented the going concern, or good-will value of its interstate business. However, as Mr. Justice Jackson pointed out on the former appeal, "to base the value (of its going concern, or good-will) on Appellant's gross revenues is to assume that every dollar of annual intake adds a dollar of intangible value to the company's assets, regardless of how much it costs in labor, interest or other expenses, including other taxes, to produce". For this obvious reason this Court then said:

> ". . . But the tax in dispute here does not depend on owning any physical property, nor upon the value thereof, but would be levied on gross revenues even if the company found some way to dispense with all local, physical property. The fact that its measure is gross revenue is consistent with a tax on the privilege of doing a volume of business which would yield that revenue, just as the Legislature indicated. *But we have declined to regard mere gross receipts as a sound measure of going-concern value in a practical world of commerce, where values depend on profitableness of a business, not merely its volume.* Cf. *United States Glue Co.* v. *Oak Creek*, 247 U. S. 321, 328-329."

If it be assumed, therefore, that Appellant's exclusive contracts with the railroads represents intangible property in the form of going-concern or good-will value subject to taxation in Virginia and should therefore have been, as Appellee contends, included in any summary of Appellant's intangible property, it is respectfully submitted that the State may not employ gross receipts as the sole measure of the value of such intangible property.

As to the stock of the Virginia company owned by Appellant, it may, at most, be said to represent the going-concern or good-will value of the intrastate business of that company as reflected by its gross receipts. These amounted in 1956 to $612,715.55 upon which the Commission assessed and the Virginia company paid a "Franchise Tax" pursuant to Sections 58-546 and 58-547 as amended in 1956, in the amount of $13,173.38. It had previously paid to Virginia without opposition, since it did solely on intrastate business in this State, License Taxes from 1933 (the year of its organization) through 1955 of $280,199.53.

Any amounts which Appellant may have received *under its contract* with the Virginia company (it has never received any dividends on its stock) were, therefore, subject to the payment of these License or Franchise Taxes which, in the view of the Commission and the Virginia Court, were imposed upon the going-concern or good-will value of the intrastate business of *that* Company. There is no basis, therefore, for Appellee's contention that the value of this intangible property should have been included in Appellant's statement of the value of *its* intangible property subject to taxation in Virginia. It should not have been since such intangible property has already been taxed against the Virginia company. The Delaware company, because of its ownership of that company, has in fact already borne the burden of that tax.

4.

Appellant's Rolling Stock Properly Included in Determining Percentage of Virginia Property Values to System Values.

There is no factual basis for the statement in Appellee's brief that the figure of $79,700,426.00 (of nationwide

depreciated system values) includes values of a class of property other than the classes located in Virginia and that, if limited to classes similar to those located in Virginia, such nationwide depreciated system values would be reduced by $15,000,000.00 (Brief p. 8). The latter figure represents the depreciated system value of Appellant's rolling stock of which amount $47,102.00 was attributed to Virginia in computing the percentage of total property values in Virginia of $475,665.00 to the depreciated system value of all of the company's property of the same classes amounting to $79,700,426.00.

It is true that the Franchise Tax in question is imposed in lieu of a State tax on Appellant's intangible property and rolling stock, but this fact has no bearing upon the question whether in determining the value of Appellant's going-concern or good-will in Virginia a disproportionate percentage of the total value of the company's properties has been attributed to this State. In fact, if Appellant's rolling stock is excluded from its depreciated system values and Virginia values of such property, the totals would represent $64,305,480.00 and $458,563.00 respectively. This would result in the Commission having attributed to the value of Appellant's property in Virginia (excluding rolling stock) 0.713% of the depreciated system value of the same kinds of property rather than 0.6% as pointed out in Appellant's "Statement as to Jurisdiction" (p. 18) with the result that 0.713% of Appellant's total property will have been considered to have a good-will or going-concern value of 1.7% of its total gross revenues.

Argument

1.

The Statute

Appellee quotes from the opinion on the prior appeal for

the purpose of demonstrating that the decision of the majority of the Court was based upon "a trinity of characteristics" which the Virginia Legislature had given the license tax then under consideration. The *practical operation* of the prior license upon Appellant was to tax it *in direct proportion to the extent to which the Commission found it had exercised the privilege of carrying on an interstate business in Virginia, namely, the amount of gross receipts derived from that business.* It was for this reason, that is, the practical operation and effect of the statute, not merely because of the "trinity of characterizations" given it by the Legislature, that this Court held the tax imposed by former Section 58-547 to be a *privilege* and not a *property* tax.

The *practical operation* of the tax presently imposed by Section 58-546, although in name a *franchise* tax, is the same as that resulting from the imposition of the prior license tax, namely, its amount as determined, not by the value of any property, *but by the extent to which Appellant carries on its interstate business in Virginia, as measured by its gross receipts.* For the same reasons, therefore, the so-called franchise tax imposed by Section 58-546 is not a property tax but is in effect a privilege tax and therefore invalid under the former decision of this Court in *Railway Express Agency, Inc.* v. *Virginia*, 347 U. S. 359, 363.

Appellee also makes reference in this connection to what was said in the "dissenting opinion" on the former appeal to the effect that "Since no one asserts that the amount of the tax is unfair or discriminatory, presumably the same tax assessed under a different name by the use of different words would be upheld." The amount of the tax was not argued by counsel on the former appeal *but its correctness was never conceded.* The discussion was directed solely to the question of the validity of the tax. In the instant case however the question of the amount of the tax was expressly

raised by counsel for Appellant and its operating report for the year 1955, introduced in evidence by counsel for the Commission, as well as Appellant's rejected Exhibits Nos. 3, 4 and 5 reveal the evidence upon which it relies in support of its present contentions in this respect. What is said in the "dissenting opinion" on the former appeal, therefore, can have no pertinent application to the record in the instant case.

2.

THE METHOD OF DETERMINING THE TAX

Appellee asserts that "the failure of the Appellant to produce evidence in the State Tribunal in support of its Claim" that it "had no way of determining and was, therefore, unable to report for taxation the amount of its gross receipts earned in interstate business passing through, into or out of Virginia, as required by Section 58-547" is sufficient reason for the Court to deny a review of the State decision.

Nothing was shown in the proceeding and nothing can be shown on this appeal, to question the correctness of Appellant's statement. It was made under oath of a responsible official and filed as a part of its report to the Commission pursuant to § 58-548 of the Virginia Code. There was, therefore, no such "failure" on its part to make a report of its gross receipts derived solely from interstate commerce as warranted the Commission's action in undertaking to determine the amount thereof under authority of § 58-549. Appellant's alleged failure was due to its inability to provide the information required since it kept no records from which it could be ascertained. *It could not affirmatively prove a fact of which it had no knowledge.* It could only state as it did under oath what it said in this connection in Appellee's

brief. Its failure to report facts of which it had no knowledge is obviously no such "failure to report" information requested by the Commission as warranted it in devising a formula for determining Appellant's gross receipts in a manner not authorized by § 58-547 of the Code.

Appellee contends that despite Appellant's "failure to produce any evidence to support its claim" in this connection, its "mathematics appear to be greatly in error" in contending that "the Virginia assessment is 'unrealistic' because 1.7% of its total gross revenues is attributed to Virginia whereas . . . there is located in Virginia only about 0.6% of its total assets of like class as those located in Virginia" (Brief p. 15).

This is said to be true because on page 8 of Appellee's Statement as to Jurisdiction it lists the various classes of property owned by it in Virginia as totaling $458,565.16 as compared with a nationwide system value of the same classes of property of $79,700,426.00 whereas, on page 18 "while using the same nationwide system value, the 'like' Virginia located property has grown to $475,665.00 (a discrepancy of over $17,000, or a little over 3%)" (Brief p. 15).

As previously pointed out the difference between the two figures to which Appellee refers is represented by the value of Appellant's rolling stock in Virginia, which, while not taxed by the Commission under the 1956 amendment to § 58-546, certainly represents property values of Appellant having taxation situs in Virginia, for the purposes of comparing the total value of its Virginia property with the system value of its properties of like kind and class.

Appellee complains of Appellant's mathematical computation of *what would have to be the value of its intangible property* ($27,947,932) in order to produce, on the basis

of the tax rate applicable to the intangible property of other public service corporations (50¢ per $100.00), a tax of $139,739.66. Appellee does not, however, appear to challenge Appellant's contention that this $28 million figure *is out of all proportion to the real going concern value of Appellant's property which the Commonwealth claims to be taxing.* Rather, it claims that in its calculations Appellant has used the wrong tax rate (50¢ per $100.00) and that, when the amount of the tax is divided by the rate of 2.15%, the going concern value of Appellant's property is found to be $6,499,519, *the same as the gross receipts it is claimed to have earned in 1955.*

This latter assertion is most revealing. It shows conclusively that *what* the Commonwealth claims *is the incidence of the tax*—the going concern value of Appellant's property—is, in fact, *the gross receipts that property can be made to produce in Virginia.* The result is, therefore, *a direct tax on gross receipts* and not a tax on *property* measured by gross receipts fairly apportioned. It is axiomatic to say that a State may not impose a direct tax on gross receipts derived solely from interstate commerce.

Moreover, it is utterly unrealistic to assert that the going concern value of Appellant's property *is exactly equal to the gross receipts earned with that property in any given year,* particularly when such gross receipts are determined on the *unit* theory by applying, as the Commission applied, the ratio of Virginia mileage to system mileage of the railroads operating in Virginia over the lines of which Appellant transported express matter. This formula gives no consideration to the value of tangible property (real and personal) of Appellant located in Virginia, the going concern value of which the Commonwealth has undertaken to determine in the manner embodied in its formula. And, in any case, gross

receipts as distinguished from net income is no proper measure of the going concern value of a taxpayer's property. *U. S. Glue Co.* v. *Oak Creek*, 247 U. S. 321.

Conclusion

For the foregoing reasons it is respectfully submitted that the two questions presented by this appeal are not only substantial but of considerable public importance and fully justify a review by this Honorable Court.

Respectfully submitted,

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